CHAPTER 21

THE REGULATORY STATE?

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1 Regulation and Governance

States can be thought of as providing, distributing, and regulating. They bake cakes, slice them, and proffer pieces as inducements to steer events. Regulation is conceived as that large subset of governance that is about steering the flow of events, as opposed to providing and distributing. Of course when regulators regulate, they often steer the providing and distributing that regulated actors supply. Governance is a wider set of control activities than government. Students of the state noticed that government has shifted from "government of a unitary state to governance in and by networks" (Bevir and Rhodes 2003, 1; Rhodes 1997). But because the informal authority of networks in civil society not only supplements but also supplants the formal authority of government, Bevir, Rhodes, and others in the networked governance tradition (notably Castells 1996) see it as important to study networked governance for its own sake, rather than as simply a supplement to government. This chapter proceeds from the assumption that there has been a rise of networked governance and builds on Jacint Jordana and David Levi-Faur's (2003, 2004) systematic evidence that, since 1980, states have become rather more

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preoccupied with the regulation part of governance and less with providing. Yet non-state regulation has grown even more rapidly, so it is not best to conceive of the era in which we live as one of the regulatory state, but of regulatory capitalism (Levi-Faur 2005).

The chapter sketches historical forces that have produced regulatory capitalism as a police economy that evolved from various feudal economies, the supplanting of police with an unregulable nineteenth-century liberal economy, then the state provider economy (rather than the "welfare state") that gives way to regulatory capitalism. In this era, more of the governance that shapes the daily lives of most citizens is corporate governance than state governance. The corporatization of the world is both a product of regulation and the key driver of regulatory growth, indeed of state growth more generally. The major conclusion of the chapter is that the reciprocal relationship between corporatization and regulation creates a world in which there is more governance of all kinds. 1984 did arrive. The interesting normative question then becomes whether this growth in hybrid governance contracts freedom, or expands positive liberty through an architecture of separated powers that check and balance state and corporate dominations. While that is the quandary of our time the chapter sets up, it does not answer it.

2 The Rise of Regulatory Studies

In the 1970s and 1980s the Chicago School could lay claim to an extraordinary swag of Nobel Prize winners such as Milton Freidman and George Stigler (1988), and preeminent law and economics scholars such as Richard Posner, who made regulation a central topic in economics. The Keynesian orthodoxies of statist remedies to market failure were supplanted by what became a Chicago orthodoxy that state failure meant the cure was worse than the disease of market failure. While from within a Chicago framework this is an odd thing to say, it is nevertheless accurate that the Chicago School studied markets as the preeminent regulatory tool. Private property rights and the price mechanism would solve problems like excessive exploitation of resources. If something like pollution was a market externality, then the most efficient way to regulate it would be to create a market in tradable pollution rights. While the Chicago intellectual dominance of these decades crowded out regulation as a topic in political science, notions of regulatory capture by the regulated industry (Bernstein 1955), carved out by political scientists decades earlier, became central to the Chicago discourse.

The Chicago School captured the political imaginations of the Carter and Reagan administrations in the USA, the Thatcher government in the UK, and beyond from the late 1970s. But over time policy-makers became cynical that if whales were endangered, either the rising price of whale meat, or property rights in whales, or creating markets in whale killing rights, were smart or dependable solutions to the problem. By the 1990s, the Chicago School ascendancy had ended and the domination of regulatory studies by economics with it. Many political scientists, including Eugene Bardach and Robert Kagan (1982), John Scholz (1991), Margaret Levi (1988), James Q. Wilson (1980), Joseph Rees (1994), Michael Moran (2003), Christopher Hood (Hood et al. 1999), Giandomenico Majone (1994), Jacint Jordana and David Levi-Faur (2004), and Peter Grabosky (1994) became leading figures in an interdisciplinary field more or less equally populated also by sociologists, criminologists, economists, accountants, and lawyers with also some interest from other disciplines, with interdisciplinary chairs in regulatory studies becoming popular recently, especially in the UK and Australia.

Regulatory studies grew with the realization that neoliberal politics had not produced privatization and deregulation, but privatization and regulatory growth. The most dominant style of research became the study of the politics of particular state regulators and self-regulators, such as those of the nuclear industry (Rees 1994), in ways that revealed the connections among private and public governance networks. In Rees' (1994) case, it is revealed how the players in this governance network were "hostages of each other;" they feared another Three Mile Island, another Chernobyl, might bring them all down.

3 The Rise of the Regulatory State?

In the first two years of the Reagan presidency there was genuine deregulatory zealotry. But by the end of the first Reagan term, business regulatory agencies had resumed the long-run growth in the size of their budgets, the numbers of their staff, the toughness of their enforcement, and the numbers of pages of regulatory laws foisted upon business (Ayres and Braithwaite 1992, 7–12). Later in the Reagan administration financial deregulation came unstuck with a Savings and Loans debacle that cost American taxpayers over $200 billion (Rosoff, Pontell, and Tillman 2002, 255). In this domain, the Reagan and Thatcher governments actually reversed direction globally as well as nationally. The Federal Reserve (US) and Bank of England led the world down to financial deregulation in the early 1980s, then led global prudential standards back up through the G-10 after the banking crises of the mid-1980s for fear of the knock-on effects foreign bank collapses could have on American business (Braithwaite and Drahos 2000, 4). The current Republican administration has presided over a 42 percent increase in regulatory staffing levels since 2001, to 242,473 full-time equivalents by 2005. Admittedly 56,000 of the increase were airport screening agents in the Transportation Security Agency (Dudley and Warren 2005, 1).

In Britain, privatization proliferated in a way that created a need for new regulatory agencies. When British telecommunications was deregulated in 1984, Oftel was created to regulate it (now Ofcom); Ofgas was born for the regulation of a privatized gas industry in 1986, OFFER for electricity in 1989 (now combined in Ofgem), OfWat for water in 1990, and the Office of the Rail Regulator (mercifully not Ofrails!) appeared in 1993 (Baldwin, Scott, and Hood 1998, 14–21). Privatization combined with new regulatory institutions is the classic instantiation of Osborne and Gaebler's (1992) prescription for reinventing government to steer rather than row. Jordana and Levi-Faur (2003, 2004) show that the tendency for state regulation to grow with privatization is a global one. As privatization spreads, they find new regulatory agencies spread even faster, and they show how the diffusion of regulatory agencies moved from the West to take off in Latin America in the 1990s.

I used to describe the key transition as one from the liberal nightwatchman state, to the Keynesian welfare state, to the new regulatory state (after 1980) and a regulatory society (see also Majone 1994; Loughlin and Scott 1997; Parker 1999; Jayasuriya 2001; Midwinter and McGarvey 2001; Muller 2002; Moran 2003). The nub of the regulatory state idea is that power is deployed "through a regulatory framework, rather than through the monopolization of violence or the provision of welfare" (Walby 1999, 123). Now I prefer Levi-Faur's (2005) adaptation of the regulatory state idea into regulatory capitalism. According to Levi-Faur, we have seen since 1980 not only what Vogel (1996) found empirically to be *Freer Markets, More Rules*, but also "more capitalism, more regulation". Privatization is part of Levi-Faur's characterization of regulatory capitalism. But it sits alongside a proliferation of new technologies of regulation and meta-regulation (Parker 2002), or control of control (Power 1997), increased delegation to business and professional self-regulation and to civil society, to intra- and international networks of regulatory experts, and increased regulation of the state by the state, much of it regulation through and for competition (Hood et al. 1999). The regulatory capitalism framework theorizes the New Public Management post-1980 as a conscious separation of provider and regulator functions within the state, where sometimes the provider functions were privatized and regulated, and sometimes they were not privatized but nevertheless subjugated to the "audit society" and government by (audited) contract (Power 1997).

The Keynesian welfare state now seems a poor description of the institutional package that dominated until 1980. One reason is that Keynes is alive and well in his influence on policy processes. Second, it is not really true that states have hollowed out; they have continued to grow as regulators as they have contracted as providers. Nor has the welfare state atrophied. Welfare state spending by rich nations has not declined (Castles 2004). Finally, the state provider economy was not just about providing welfare; it was about states providing transport, industrial infrastructure, utilities, and much more beyond welfare, a deal of which was privatized in the transition to regulatory capitalism.

Even the idea of the nightwatchman state of the nineteenth century needs qualification. The prehistory of the institutional change summarized in this paper could be described as a transition from various feudalisms to a police economy. The sequence I will describe is a transition then from that police economy to the unregulable economy tending to laissez-faire after the collapse of police, to the "state provider economy" (rather than the "welfare state") to "regulatory capitalism" (rather than the "regulatory state").

4 The Police Economy

What does Tomlins (1993, 37–8) mean when he says that writing a history of the American state without a reference to the genealogy of "police" is "akin to writing a history of the American economy without discussing capitalism?" In white settler societies it is easier to see with clarity the police economy because it did not have to struggle to supplant the old economy of monopolies granted by the king to guilds, market towns, and trading companies like the Hudson Bay Company (even as the New World was partly constituted by the latter). That economy of monopoly domination granted by the king was not only an earlier development in the transition from feudalism to capitalism that was subsequently (de)regulated by police, it was also a development largely restricted to cities which were significant nodes of manufactures and long-distance trade.[1] Tiny agricultural communities that did not have a guild or a chartered corporation had a constable. The early modern idea of police differs from the contemporary notion of an organization devoted to fighting crime (Garland 2001). Police from the sixteenth to the nineteenth century in continental Europe meant institutions for the creation of an orderly environment, especially for trade and commerce. The historical origins of the term through German back to French is derived from the Greek notion of "policy" or "politics" in Aristotle (Smith 1978, 486; Neocleous 1998). It referred to all the institutions and processes of ordering that gave rise to prosperity, progress, and happiness, most notably the constitution of markets. Actually it referred to that subset of governance herein conceived as regulation.

[1] France was an exception that made guilds state organs and spread their regulatory authority out from towns across the entire countryside (Polanyi 1957, 66).

Police certainly included the regulation of theft and violence, preventive security, regulation of labor, vagrancy, and the poor, but also of weights and measures and other forms of consumer protection, liquor licencing, health and safety, building, fire safety, road and traffic regulation, and early forms of environmental regulation. The institution was rather privatized, subject to considerable local control, relying mostly on volunteer constables and watches for implementation, heavily oriented to self-regulation, and infrequent (even if sometimes draconian) in its recourse to punishment. The *lieutenant de police* (a post established in Paris in 1667) came to have jurisdiction over the stock exchange, food supplies and standards, the regulation of prostitutes, and other markets in vice and virtue. Police and the "science of police" that in eighteenth-century German universities prefigured contemporary regulatory studies sought to establish a new source of order to replace the foundation laid by the estates in the feudal order that had broken down.

English country parishes and small market towns, as on the Continent, had constables and local watches under a Tudor system that for centuries beyond the Tudors regulated the post-feudal economic and social order. Yet there was an English aversion to conceptualizing this as police in the French, German, and Russian fashion. The office of the constable had initially been implanted into British common law and institutions by the Norman invasion of 1066. The office was in turn transplanted by the British to New England, with some New England communities then even requiring Native American villages to appoint constables. Eighteenth-century English, but not American, political instincts were to view Continental political theory of police as a threat to liberty and to seek a more confined role for the constable. Admittedly, Blackstone in his fourth volume of *Commentaries on the Laws of England* (1769 [1966]) adopts the Continental conception of police, and Adam Smith applauds it in his *Lectures on Jurisprudence* (1762–4 [1978]). But Neocleous (1998, 444) detects a shift from the Smith of the *Lectures* to the *Wealth of Nations*, both of which discuss police and the pin factory. The shift is from seeing:

> police power contributing to the wealth-producing capacities of a *politically constituted* social order to being a site of autonomous social relations—the independent factory employing independent wage-labourers within a *laissez faire* economy.

Polanyi (1957, 66) quotes Montesquieu as sharing the early Smithian view of English police as constitutive of capitalism, when he says in the *Spirit of Laws* that "The English constrain the merchant, but it is in favor of commerce." Even as institutions of eighteenth-century police are to a considerable degree in place in the nations that become the cutting edge of capitalism (this is also true of the extremely effective policing of the Dutch Republic (Israel 1995, 677–84)), the leading interpreters of capitalism's success move from an interpretation of markets constituted by police to laissez-faire markets.

Peel's creation of the Metropolitan Police in London in 1829 and the subsequent creation of an even more internationally influential colonial model in Dublin were watersheds.

Uniformed paramilitary police, preoccupied with the punitive regulation of the poor to the almost total exclusion of any interest in the constitution of markets and the just regulation of commerce, became one of the most universal of globalized regulatory models. So what happened to the business regulation? From the mid-nineteenth century, factories inspectorates, mines inspectorates, liquor licensing boards, weights and measures inspectorates, health and sanitation, food inspectorates, and countless others were created to begin to fill the vacuum left by constables now concentrating only on crime. Business regulation became variegated into many different specialist regulatory branches. The nineteenth-century regulatory growth is more in the number of branches than in their size and power. Laissez-faire ideology underpinned this regulatory weakness. The regulators' feeble resourcing compared to the paramilitary police, and the comparative wealth of those they were regulating, made the early business regulators even more vulnerable to capture and corruption than the police, as we see with poorly resourced business regulators in developing economies today.

5 The Unregulable Liberal Economy

Where problems were concentrated in space, nineteenth-century regulation secured some major successes. Coal mines became much safer workplaces from the latter years of the nineteenth century, as did large factories in cities (Braithwaite 1985), regulatory transitions that are yet to occur in China that today accounts for 80 percent of the world's coal mine fatalities. Rail travel was causing thousands of deaths annually in the USA late in the nineteenth century (McCraw 1984, 26); by the twentieth century it had become a very safe way to travel (Bradbury 2002). Regulation rendered ships safer and more humane transporters of exploited labor (slaves, convicts, indentured labor, refugees from the Irish famine) to corners of the empire suffering labor shortages (MacDonagh 1961). The paramilitary police were also successful in assisting cities like London, Stockholm, and Sydney to become much safer from crimes against persons and property for a century and a half from 1820 (Gurr, Grabosky, and Hula 1977). But it was only problems like these that were spatially concentrated where nineteenth-century regulation worked. In most domains it worked rather less effectively than eighteenth-century police. This was acceptable to political elites, who were mainly concerned to make protective regulation work where the dangerous classes might congregate to threaten the social order—in cities, convict ships, factories.

In addition to the general under-resourcing of nineteenth-century regulatory inspectorates, the failure to reach beyond large cities, the capture and corruption, there was the fact that the inspectorates were only beginning to invent their regulatory technologies for the first time. They were still learning. The final and largest limitation that made their challenge impossible was that in the nineteenth century almost all commerce was small business. It is harder for an inspector to check ten workplaces employing six people than one with sixty workers. This remains true today. We will see that the regulatory reach of contemporary capitalism would be impossible without the lumpiness of a commerce populated by big businesses that can be enrolled to regulate smaller businesses. Prior to the nineteenth century, it was possible to lever the self-regulatory capabilities of guilds in ways not dissimilar to twentieth-century capabilities to enrol industry associations and big business to regulate small business. But the well-ordered world of guilds had been one of the very things destroyed by the chaotic emergence of laissez-faire capitalism outside the control of such premodern institutions. Where guilds did retain control, capitalism did not flourish, because the guilds restricted competition.

While the nineteenth-century state was therefore mostly a laissez-faire state with limited reach in its capacity to regulate, it was a state learning to regulate. While the early nineteenth-century tension was between the decentralized police economy and laissez-faire liberalism, the late-century tension was between laissez-faire and the growth of an administrative state of office blocks in large cities.

6 The Unregulable Liberal Economy Creates the Provider State

A simple solution to the problem of private rail companies charging monopoly prices, bypassing poorer towns, failing to serve strategic national development objectives, and flouting safety standards, was to nationalize them. A remedy to unsanitary private hospitals was a public hospital system that would make it unnecessary for patients to resort to unsafe private providers. The challenge of coordinating national regulation of mail services with international regulation through the Universal Postal Union (established in 1863) rendered a state postal monopoly the simplest solution to the coordination that was otherwise beyond the unregulable nineteenth-century liberal economy. The spread of socialist ideas during the nineteenth century gave an ideological impetus to the provider state solution. Progressively, until the beginning of the second half of the twentieth century, the provider state model proliferated, especially in Europe, with airlines, steel, coal, nuclear power, urban public transport, electricity, water, gas, health insurance, retirement insurance, maternal and child welfare, firefighting, sewerage, and countless other things being provided by state monopolies.

Bismarck consciously pursued welfare state provision as a strategy for thwarting the growing popularity of the idea of a socialist revolution to replace capitalism entirely with a state that provided everything. Lloyd-George was impressed by Bismarck's diagnosis and the British Liberal Party also embraced the development of the welfare state, only to be supplanted by a Labour Party that outbid the Liberals with the state provision it was willing to provide to workers who now had votes and political organization.

While many of these state takeovers also occurred in the United States during the century and a half that preceded the arrival of regulatory capitalism, the scope of what was nationalized was narrower there. One reason was that trade unions and the parties and ideologies they spawned were weaker in the USA during the twentieth century. There were periods up to the first decade of the twentieth century when trade unions in the United States were actually numerically and politically stronger than in Europe. The big businesses that grew earlier in the United States used their legal and political capabilities to crush American unionism in the late nineteenth and early twentieth century, frequently through the murder of union officials and threats of violence (Braithwaite and Drahos 2000, 229). American big business could simply organize more effectively against the growth of trade unions and the provider state ideologies they sponsored than against the smaller family firms that predominated in Europe.

A paradox of the fact that American business culture moderated the growth of the provider state was that the regulatory state grew more vigorously in the USA, especially during the progressive era (1890–1913) (which saw the creation of the Federal Trade Commission, Food and Drug Administration, and Interstate Commerce Commission, among other agencies) and the New Deal (1930s) (which saw the creation of the Securities and Exchange Commission, the National Recovery Administration, the Federal Communications Commission, the Civil Aeronautics Board, among others) (McCraw 1984). Building paradox upon paradox, the growth in the sophistication of regulatory technologies in the USA showed that there were credible alternatives to the problems the provider state set out to solve. The New Deal also supplied an economic management rationale to an expansive state. Keynes' general theory was partly about increasing public spending to stimulate an economy when it was in recession, as it was at the time of the New Deal.

7 Regulation Creates Big Business

Braithwaite and Drahos (2000) have described the corporatization and securitization of the world as among its most fundamental transformations of the last three centuries. I will summarize here how this was enabled by regulation, but then how corporatization in turn enabled regulatory capitalism to replace the provider state economy. Corporations existed for more than a millennium before securities. For our purposes, a security is a transferable instrument evidencing ownership or creditorship, as a stock or bond. The legal invention of the security in the seventeenth century was the most transformative movement in the history of corporations. It enabled the replacement of family firms with very large corporations based on pooled contributions of capital from thousands of shareholders and bondholders. These in turn enabled the great technological projects of eighteenth- and nineteenth-century capitalism—the railroads, the canals, the mines.

When it was first invented, however, the historical importance of the security had nothing to do with the corporatization of the world. Rather, it transformed state finances through bonds that created long-term national debts. While the idea of dividing the national debt into bonds was invented in Naples in the seventeenth century, it was England that managed by the eighteenth century to use the idea in a financial revolution that helped it gain an upper hand over its principal rival, France (Dickson 1993). England became an early provider state in a particularly strategic way by seizing full national control of public finance: formerly private tax and customs collecting were nationalized in the seventeenth century, a Treasury Board was established in the eighteenth, and finally the Bank of England was given national regulatory functions. The Treasury Board realized that the national debt could be made, in effect, self-liquidating and long-term, protecting the realm from extortionate interest rates at times of war and the kind of vulnerability that had brought the Spanish empire down when short-term loans had to be fully repaid after protracted war. Instead of making England hostage to Continental bankers, the national debt was divided into thousands of bonds, with new bond issues placed on the market to pay for old bonds that were due to be paid.

Securitization paid for the warships that allowed Britannia to rule the waves, to trade and colonize—to be a state provider of imperial administration and national as opposed to feudal security on a scale not imagined before. Today, of course, national debts can no longer be used to rule the world because they are regulated by other states through the Paris Club and the IMF (International Monetary Fund). The key thing here is that the early providers of state control of public finance in the process also induced a private bond market. This created the profession of stockbroking and the institution of the stock exchange. For most of the period when Amsterdam and London were the leading stock exchanges in the world, they were predominantly trading securities in the debts of nations. Gradually this created a market in private stocks and bonds. These enabled the English to create the Massachusetts Bay Company, the Hudson Bay Company, the British South Africa Company, the East India Company, and others that conquered the world, and the Dutch to create an even more powerful East India Company and the United New Netherland Company that built a New Amsterdam which was to succeed London as the next capital of the world.

State creation of a London market in the broking of securities fomented other kinds of securities exchanges as well, the most important of which was Lloyd's of London. Britannia's merchant fleet ruled the waves once an efficient market in spreading the lumpy risk of ships sinking with valuable cargos was created from a base in Lloyd's Coffee Shop. Lloyd's in turn became an important inventor of regulatory technologies that made regulatory capitalism possible in advance of the supplanting of the provider state with regulatory capitalism. For example, in building a global reinsurance market, it invented the plimsoll line that allowed insurers to check by simple observation at ports whether ships arrived overloaded.

But by far the most important impact of securitization was that it began a process, that only took off quite late in the nineteenth century, of replacing a capitalism of family firms with one of professional managers of securities put in their trust by thousands of shareholders. Even in New York, where the corporatization of the world was most advanced, it was not until the third decade of the twentieth century that the majority of litigants in appellate courts were corporations rather than individual persons and the majority of actors described on the front page of the *New York Times* were corporate rather than individual actors (Coleman 1982, 11).

8 Antitrust Globalizes American Mega-corporate Capitalism

In the 1880s, predominantly agrarian America became deeply troubled by the new threat to what they saw as their Jeffersonian agrarian republic from concentrations of corporate power that they called trusts. Farmers were especially concerned about the "robber barons" of railroads that transported their produce across the continent. But oil, steel, and other corporate concentrations of power in the northeast were also of concern. Because Jeffersonian republicanism also feared concentrations of state power in the northeast, the American solution was not to nationalize rail, oil, and steel. It was to break up the trusts. By 1890 at least ten US states had passed antitrust laws, at which point the Sherman Act was passed by a virtually unanimous vote of the US Congress.

The effect of enforcement of the Sherman Act by American courts was not exactly as intended by the progressive era social movement against the railroad, oil, steel, and tobacco trusts. Alfred Chandler (1977, 333–4) noted that "after 1899 lawyers were advising their corporate clients to abandon all agreements or alliances carried out through cartels or trade associations and to consolidate into single, legally defined enterprises." US antitrust laws thus actually encouraged mergers instead of inhibiting them, because they "tolerated that path to monopoly power while they more effectively outlawed the alternative pathway via cartels and restrictive practices" (Hannah 1991, 8). The Americans found that there were organizational efficiencies in managerially centralized, big corporations that made what Chandler (1990, 8) called a "three-pronged investment:" (1) "an investment in production facilities large enough to exploit a technology's potential economies of scale or scope;" (2) "an investment in a national and international marketing and distribution network, so that the volume of sales might keep pace with the new volume of production;" and (3) "to benefit fully from these two kinds of investment the entrepreneurs also had to invest in management."

According to Freyer's (1992) study in the Chandler tradition, the turn-of-the-century merger wave fostered by the Sherman Act thrust US long-term organization for economic efficiency ahead of Britain's for the next half-century, until Britain acquired its Monopolies Act 1948 and Restrictive Trade Practices Act 1956. Until the 1960s, the British economy continued to be dominated by family companies that did not mobilize Chandler's three-pronged investment. Non-existent antitrust enforcement in Britain for the first half of the twentieth century also left new small business entrepreneurs more at the mercy of the restrictive business practices of old money than in the USA. British commitment to freedom of contract was an inferior industrial policy to both the visible hand of American lawmakers' rule of reason and the administrative guidance of the German Cartel Courts. For the era of managerial capitalism, liberal deregulation of state monopolies formerly granted to Indies Companies and guilds was not enough. Simple-minded Smithean invocation of laissez-faire missed the point. A special kind of regulation for the deregulation of restrictive business practices was needed which tolerated bigness.

Ultimately, Braithwaite and Drahos (2000) show that this American model of competitive mega-corporate capitalism globalized under four influences:

1. Extension of the model throughout Europe after the Second World War under the leadership of the German anti-cartel authority, the *Bundeskartelamt*, a creation of the American occupation.
2. Cycles of Mergers and Acquisitions (M&A) mania in Europe catalyzed in part by M&A missionaries from American law firms.

3. Extension of the model to the dynamic Asian economies in the 1980s and 1990s, partly under pressure from bilateral trade negotiations with the USA and Europe (who demanded breaking the restrictive practices of Korean *chaebol*, for example).
4. Extension of the model to developing countries with technical assistance from organizations such as UNCTAD (United Nations Conference on Trade and Development), prodded by the IMF good governance agenda.

This history of a regulatory capitalism that promotes competition among large corporations dates from the 1880s for the US but is very recent for other states. Most of the world's competition regulators have been created since 1990. There were barely twenty in the 1980s; today there are approximately 100.

9 Mega-corporate Capitalism Creates Regulatory Capitalism

The regulatory state creates mega-corporations, but large corporations also enable regulatory states. We have seen that antitrust regulation is the primary driver of the first side of this reciprocal relationship. But other forms of regulation also prove impossible for small business to satisfy. In many industry sectors, regulation drives small firms that cannot meet regulatory demands into bankruptcy, enabling large corporates to take over their customers (see, for example, Braithwaite's (1994) account of how tougher regulation drove the "mom and pops" out of the US nursing home industry in favor of corporate chains). For this reason, large corporations often use their political clout to lobby for regulations they know they will easily satisfy but that small competitors will not be able to manage. They also lobby for ratcheting up regulation that benefits them directly (e.g. longer patent monopolies) but that are mainly a cost for small business (Braithwaite and Drahos 2000, 56–87).

To understand the second side of this reciprocal relationship more clearly—mega-corporates create regulatory capitalism—consider the minor example of the regulation of the prison industry (Harding 1997). It is minor because most countries have not taken the path of privatizing prisons, though in the USA, where prisons house more than two million inmates and employ about the same number, it is not such a minor business. In the 1990s many private prisons were created in Australia, a number of them owned by the largest American prison corporations. A question that immediately arose was how was the state to ensure that American corporations met Australia's national and international human rights obligations. When the state was the monopoly provider of prison places, it simply, if ineffectively, told its civil servants that they would lose their jobs if they did not fulfill their duty in respect of such standards. This requirement was put into contracts with the private prisons. But then the state has little choice but to invest in a new regulatory agency to monitor contract compliance.

As soon as it puts this in place, prisoner rights' advocates point out that in some respects the old state-run prisons are more abusive than the new private providers, so the prison inspectorate should monitor the public prisons. Moreover, it should make public its reports on the public prisons so that transparency is as real there as with private prisons (Harding 1997). Of course, the private corporations lobby for this as well to create a "level playing field" in their competition with the state. Hence, the corporatization of the prison industry creates not only a demand for the independent, publicly transparent regulation of the corporates, it also creates a potent political demand for regulation of the state itself. This is central to understanding why the regulatory state is not the correct descriptor of contemporary transformations; regulatory capitalism involves heightened regulation of the state as well as growth in regulation by the state (Hood et al. 1999). We have seen this in many other domains including the privatization of British nursing home provision described earlier which led to the inspection of public nursing homes.

Security generally has been a major domain of privatization. Most developed economies today have a ratio of more than three private police to one public police officer (Johnston and Shearing 2003). Under provider capitalism it was public police officers who would provide security at football stadiums, shopping complexes, universities, and airports. But today, as we move from airport to shops to leisure activity to work, we move from one bubble of private security to another (Shearing and Wood 2003; Johnston and Shearing 2003). If our purse is stolen at the shopping mall, it is a private security officer who will come to our aid, or who will detain us if we are caught shoplifting. The public police will only cover us as we move in the public spaces between bubbles of private security. As with prisons, public demand for regulation of the private security industry arises when high profile incidents occur, such as the recent death of one of Australia's most talented cricketers after a bouncer's punch outside a nightclub.

International security has also been privatized. Some of those allegedly leading the abuses at Abu-Grahib in Iraq were private security contractors. Many of these contractors carry automatic weapons, dress like soldiers, and are killed as soldiers by insurgents. In developing countries, particularly in Africa, military corporations have been hired to be the strike infantry against adversaries in civil wars. An estimated 70 per cent of the former KGB found employment in this industry (Singer 2002). This has led the British government to produce a White Paper on the need to regulate private military organizations and to the quip that the regulator be dubbed OfKill!

So the accumulation of political power into the hands of large private corporations creates public demand for regulation. Moreover, we have seen that the largest corporations often demand this themselves. In addition, the regulatory processes and (partly resultant) competitive imperatives that increase the scope and scale of corporations make what was unregulable in the nineteenth century, regulable in the twentieth. The chemicals/pharmaceuticals industry, for example, creates a huge public demand for regulation. Incidents like Bhopal with the manufacture of agricultural chemicals and thalidomide with pharmaceuticals, that kill thousands, galvanize mass concern. The nineteenth-century regulatory state could only respond to public outrage by scapegoating someone in the chemical firm and throwing them in prison. It was incapable of putting a regulatory regime in place that might prevent a recurrence by addressing the root causes of disasters. There were too many little chemical producers for state inspectors to monitor and it was impossible for them to keep up with technological change that constantly created new risks.

After the Bhopal disaster, which ultimately caused the demise of Union Carbide, the remaining large chemical producers put in place a global self-regulatory regime called "Responsible Care," with the objective of averting another such disaster that might cause a multinational to go under leaving a stain on the reputation of the entire industry (Moffet, Bregha, and Middelkoop 2004). That's all very well, the regulatory cynic notes, but it still remains the case today that most chemical risks are posed by small, local firms with poor self-regulatory standards, not by the multinationals. Yet the fact of mega-corporate capitalism that has evolved over the past century is that almost all small chemical firms are linked upstream or downstream to one multinational or another. They buy or sell chemical ingredients to or from the large corporates. This fact creates a mass tort risk for the multinationals. The multinationals are the ones with the deep pockets, the high public profile, and brand reputation; so they are more vulnerable to the irresponsibility of small chemical firms linked to them than are those firms themselves. So Responsible Care requires large firms to sustain a chain of stewardship for their chemicals upsteam and downstream. This has the effect of making large corporations the principal regulators of small chemical firms, not the state. This is especially so in developing countries where the temptations of state laissez-faire can make the headquarters' risks potentially most catastrophic.

State regulation and private regulation through tort creates larger chemical corporations. We see this especially in pharmaceuticals where the costs of testing new drugs now run to hundreds of millions of dollars. Global scandals that lead to demand for still tougher regulation creates a community of shared fate among large firms in the industry (note Rees's (1994) study of how the Three Mile Island disaster created a community of fate in the nuclear industry, a belief that another Three Mile Island could cripple the entire industry). Big business responds to finding itself in a community of fate in a risk society (Beck 1992) by industry-wide risk management. This implies managing upstream and downstream risks. Again we see that regulatory capitalism is not only about the regulatory state, though this is a big part of the chemicals, pharmaceuticals, and nuclear stories. It is also about regulation by industry associations of their large members and regulation of small producers by large producers who share the same chain of stewardship for a risk. At the end of the day, it is not only states (with technical assistance from international organizations like the World Health Organization and the OECD (Organization for Economic Co-operation and Development)) doing the regulating; it is global and national industry associations and large multinational firms. Not only does this ease some of the logistical burdens upon the regulatory state in monitoring a galaxy of small firms, it also eases some of the information problems that made chemicals unregulable in the nineteenth century. As partners in regulatory capitalism, state regulators can lean on Responsible Care, the OECD, and large multinationals that may know more than them about where new chemical risks are emerging. Of course there is debate about how well these private–public partnerships of regulatory capitalism work (Gunningham and Grabosky 1998).

Braithwaite and Drahos (2000) revealed the importance of yet other actors who are as important as non-state regulators. Ratings agencies like Moody's and Standards and Poors, having witnessed the bankrupting of imprudent chemical producers, downgrade the credit rating of firms with a record of sloppy risk management. This makes money more expensive for them to borrow. Reinsurers like Lloyd's also make their risks more expensive to reinsure. The cost and availability of lending and insurance also regulates small firms. Care homes (including nursing homes) frequently go bankrupt in the UK; these bankruptcies are often connected to the delivery of poor quality care. Reports of British government care home inspections are on the Internet. When homes approach banks for loans, it is good banking practice today to do an Internet check to see if the home has any looming quality of care problems. If it does, banks sometimes refuse loans until these problems are addressed. Banks have thence become important regulators of little and large British care home firms.

9.1 Corporatization, Tax, and the Constitution of Provider and Regulatory Capitalism

One effect of the corporatization of capitalism in the twentieth century was that it made it easier for the state to collect tax. This revenue made it possible to fund both the provider state and the regulatory state. State provision of things like welfare and transport, and state regulation are expensive activities. So taxpaying becoming regulable was decisive to the subsequent emergence of the provider state and regulatory capitalism. In most developing societies taxpaying remains unregulable and this has closed the door on credible state provision and state regulation.

Of course it is more cost-effective to collect tax from one large corporation than ten small ones and most corporate tax is collected from the largest 1 percent of corporations in wealthy nations. But this is not the main reason that corporatization created a wealthy state. More fundamentally, corporatization assisted the collectability of other taxes (see Braithwaite and Drahos 2000, ch. 9). As retailing organizations became larger corporates, as opposed to family-owned corner stores, the collection of indirect tax became more cost-effective. When most of the Australian working class was rural, itinerantly shearing sheep for graziers, cutting cane, or picking fruit, collecting taxes from them was difficult and costly. But as the working class became progressively more urban—in the employ of city-based corporations—income tax collections from workers became a goldmine, especially after the innovation of Pay As You Earn (withholding of tax from pay packets by employers, which started in Australia in 1944). The final contribution of mega-corporatization was financial institutions becoming more concentrated and computerized, making withholding on interest and dividends feasible. So tax on salary income, corporate tax, sales taxes, and tax on income from interest and dividends all became more collectable. The result was that, contrary to the fairytale of neoliberalism, the state grew and grew into a regulatory capitalism where the state both retained many of its provider functions and added many new regulatory ones.

Pay As You Earn was an innovative regulatory technology of wider relevance. PAYE taxpayers cannot cheat because it is not them, but their employers, who hand over the money. Theoretically of course the employer can cheat. But they have no incentive to do so, since only their employee benefits from the cheating, and the cheating is visible in the accounts. The regulatory strategy of general import here is to impose regulatory obligations on keepers of a gate that controls the flow of the regulated activity, where the gatekeepers do not benefit personally from opening and closing the gate. This not only separates the power from the incentive to cheat, it also economizes on surveillance. It is not necessary to monitor all the regulated actors at all times. The regulator must only monitor the gatekeeper at those points when gates can be unlocked.

10 The Regulated State

For 90 percent of the world's states there are large numbers of corporations with annual sales that exceed the state's GDP. The CEOs of the largest corporations typically are better networked into other fonts of power than the presidents of medium-sized states. Consequently large corporations do a lot of regulating of states. There are also some smaller global corporations like Moody's and Standard and Poors that have specialized regulatory functions over states—setting their credit ratings. More generally, finance capital holds sway over states. This is exercised through capital movements, but also through lobbying global institutions such as the IMF, the Basle Committee, World Trade Organization Panels, and the World Bank, who might have more direct control over a specific sphere of state activity. The most formidable regulator of debtor states is the IMF, as a result of its frequently used power to impose regulatory conditions upon debt repayment.

While states have formidable regulatory leverage over airlines, for example, airlines can enrol the International Civil Aviation Organization to regulate landing rights to and from states that fail to meet their obligations to the orderly conduct of international transport. While states regulate telecoms, they must submit to regulation by the ITU (International Telecommunication Union) if they want interconnectivity with telecoms in other states, and powerful corporations invest heavily in lobbying the ITU and in having their executives chair its technical committees.

Many states simply forfeit domains of regulation to global corporations that have superior technical capability and greater numbers of technically competent people on the ground. For example, in many developing nations the Big Four accounting firms effectively set national accounting standards. States are also regulated by international organizations (and bilaterally) to comply with legal obligations under treaties they have signed. Sanctions range from armed force to air and sea blockades, suspension of voting rights on international organizations, trade sanctions, and "smart sanctions" such as seizure of foreign assets and denial of visas to members of the regime and their families. Regional organizations such as the EU (European Union) and the African Union, of course, also have a degree of regulatory leverage over member states. Leverage tends to be greatest when states are applying for membership of an international club such as the World Trade Organization or EU from which they believe they would benefit.

One of the defining features of regulatory capitalism is that parts of states are set up with independent capacities to regulate other parts of the state. Since 1980 the globalization of the institution of the Ombudsman and the proliferation of audit offices has reached the point where some describe what Levi-Faur calls regulatory capitalism as *The Audit Society* (Power 1997). Finally, there is the development of independent inspectors of privatized industries moving their oversight back to public provision.

Of course the idea of a separation of powers where one branch of governance regulates another so that neither executive, judiciary, nor legislature can dominate governance is an old one, dating at least from the Spartan constitution and Montesquieu (Braithwaite 1997). But practice has become more variegated, especially in Asian constitutions such as those of Thailand and Taiwan that conceive of themselves as having more than three branches of governance, with branches such as the Election Commission, Ombudsman, Human Rights Commission, Counter Corruption Commission, and Audit and Examination Offices enjoying constitutionally separated powers from the legislative, executive, and judicial branches. The theory as well as the practice of the doctrine of separation of powers under regulatory capitalism has also moved forward on how innovative separations of powers can deter abuse of power (see Braithwaite 1997). To the extent that there are richer, more plural separations within and between private and public powers in a polity, there is a prospect of moving toward a polity where no one power can dominate all the others and each power can exercise its regulatory functions semi-autonomously even against the most powerful branch of state or corporate power. As Durkheim began to see, the art of government "consists largely in coordinating the functions of the various self-regulating bodies in different spheres of the economy" (Schepel 2005, ch. 1; see also Cotterrell 1999; Durkheim 1930, preface).

11 Conclusion

The transitions since feudal structures of governance fell to incipient capitalist institutions have been from a police economy, to an unregulable nineteenth-century liberal economy that oscillated between laissez-faire, dismantling the decentralized police economy, and laying the bricks and mortar of an initially weak urban administrative state, to the provider state economy, to regulatory capitalism. Across all of these transitions, markets in fits and starts have tended to become progressively more vigorous, as has investment in the regulation of market externalities. Not only have markets, states, and state regulation become more formidable, so has non-state regulation by civil society, business, business associations, professions, and international organizations. Separations of powers within polities have become more variegated, with more private–public hybridity. This means political science conceived narrowly as a discipline specialized in the study of public governance to the exclusion of corporate governance, NGO governance, and the governance of transnational networks makes less sense than it once did. If we have entered an era of regulatory capitalism, regulation may be, in contrast, a fruitful topic around which to build intellectual communities and social science theory.

Interesting agendas implied by this perspective are empirical studies of how networked regulators like the Forest and Marine Stewardship Councils, Social

Accountability International, and the Sustainable Agriculture Network (Courville 2003) operate, research on devolved regulatory technologies that harness local knowledge (Shearing and Wood 2003), Levi Faur's (2006) agenda of documenting and comparatively dissecting the *Varieties of Regulatory Capitalism*, the Hall and Soskice (2001), Stiglitz (2002), and Rodrik (2004) agendas of diagnosing the institutional mixes that make capitalism buzz and collapse in the context of specific states, the Dorf and Sabel (1998) agenda of evidence-based "democratic experimentalism," the Campbell Collaboration, and behavioral economics agendas for real policy experiments on the impacts of regulatory interventions. Important among these are experiments on meta-regulation—regulated self-regulation—as a form of social control that seems paradigmatic of regulatory capitalism (Parker 2002; Braithwaite 2005).

In seeing the separations among the periods posited in this chapter, it is also important to grasp the posited continuities. Both markets and the state become stronger, enlarged in scope and transaction density, at every stage. Elements of eighteenth-century police are retained in the creation of nineteenth-century paramilitary police and other specialized regulators. Post-1980 regulatory capitalism learns from and builds upon the weaknesses (and the strengths) of nineteenth- and early twentieth-century regulation—from twenty-first-century private security corporations learning from Peel's Metropolitan Police and the KGB, to state shipping regulators and the International Maritime Organization learning from regulatory technologies crafted in Lloyd's Coffee Shop. While many problems solved by state provision prior to 1980 are thence solved by privatization into contested, regulated markets, most of the state provision of the era of the provider state persists under regulatory capitalism. Even some renationalization of poorly conceived privatization has begun.

A contribution of this chapter has been to suggest that regulation, particularly antitrust and securitization of national debt, enabled the growth of both provider and regulatory states. Regulation did this through pushing the spread of large corporations that made Chandler's (1977, 1990) three-pronged investment. The corporatization of the world increased the efficacy of tax enforcement, funding provider and regulatory state growth. The corporatization of the world drove a globalization in which transnational networks, industry associations, professions, international organizations, NGOs, NGO/retailer hybrids like the Forest Stewardship Council, and most importantly corporations themselves (especially, but not limited to, stock exchanges, ratings agencies, the Big Four accounting firms, multinationals that specialize in doing states' regulation for them like Société Général de Surveillance,[2] and large corporates that regulate small upstream and

[2] This is a large Swiss multinational that provides all manner of regulatory services for states from environmental inspection to collecting nations' customs duties for them in innovative ways (Braithwaite and Drahos 2000, 492–3).

downstream firms in the same industry) became important national, regional, and global regulators. This was a very different capitalism and a very different world of governance than existed in the early twentieth-century industrial capitalism of family firms. Hence the power of Levi-Faur's conceptualization of regulatory capitalism. While states are "decentred" under regulatory capitalism, the wealth it generates means that states have more capacity both to provide and to regulate than ever before.

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